Ninepoint Focused Global Dividend Class

July 2019 Commentary

Investment Team

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Year-to-date to July 31, the Ninepoint Focused Global Dividend Class generated a total return of 15.25% compared to the S&P Global 1200 Index, which generated a total return of 12.65%. For the month, the Fund generated a total return of 1.42% while the Index generated a total return of 0.73%. After a solid recovery rally to start the year, markets faltered in May as US-China trade negotiations broke down. However, sentiment improved dramatically through June and July with what appeared to be a truce in the trade war, reasonable second quarter results and dovish reassurances from global Central Banks.

Unfortunately, investors may have gotten ahead of themselves in terms of monetary stimulus expectations and a dovish ECB meeting on July 25 (but without concrete action) and a 25-bps interest rate cut from the US Fed on July 31 (instead of either a 50-bps interest rate cut or 25-bps interest rate cut and clarity on incremental easing) disappointed the market. But keep in mind that the ECB will likely act more aggressively at its next policy meeting and the US Fed funds futures are currently indicating a 100% chance of an interest rate cut on September 18, providing further accommodation and ensuring an extended economic cycle.

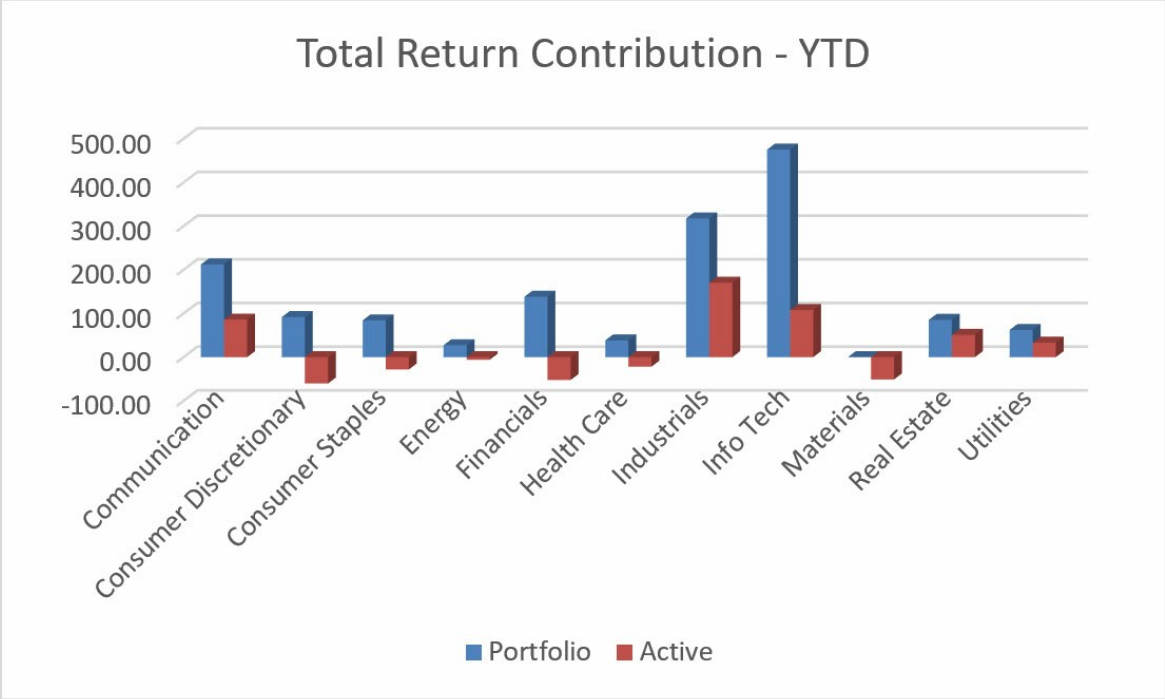
On a positive note, with 90% of the companies in the S&P 500 reporting actual results, 75% of companies have reported a positive earnings surprise and 57% have reported a positive revenue surprise, according to FactSet. On a blended basis (combines actual results for companies that have reported and estimated results for companies that have yet to report), the earnings growth rate is coming in at -0.7% and the revenue growth rate is coming in at 4.1%, but both measures have been improving through the earnings season. Importantly, companies with greater US domestic exposure have reported much better revenue and earnings growth rates than those with greater international sales.

We remain concerned that the global PMIs have yet to rebound, with the JPMorgan Global Manufacturing PMI particularly weak in July at 49.3, its lowest level since October 2012. Consistent with global growth concerns, the US 10-year Treasury yield has fallen below 2.0% and the US 2-year to 10-year yield curve, again a widely-watched recession indicator, remains flat (but not yet inverted). Accommodative monetary policy, easing trade tensions and the passage of time will be required to return to more robust economic growth, hence the market's fixation on US Fed Chairman Powell's every word and President Trump's every tweet.

We continue to believe that the current environment will prove to be a mid-cycle slowdown and we will avoid a global recession. If we follow the roadmap of past cycles, interest rates should decline, global PMIs should bottom and earnings expectations for 2020 should inflect higher in turn. Forward earnings growth coupled with multiple expansion should allow the broad equity markets to rally until monetary conditions need to be tightened to offset inflationary pressure. We believe

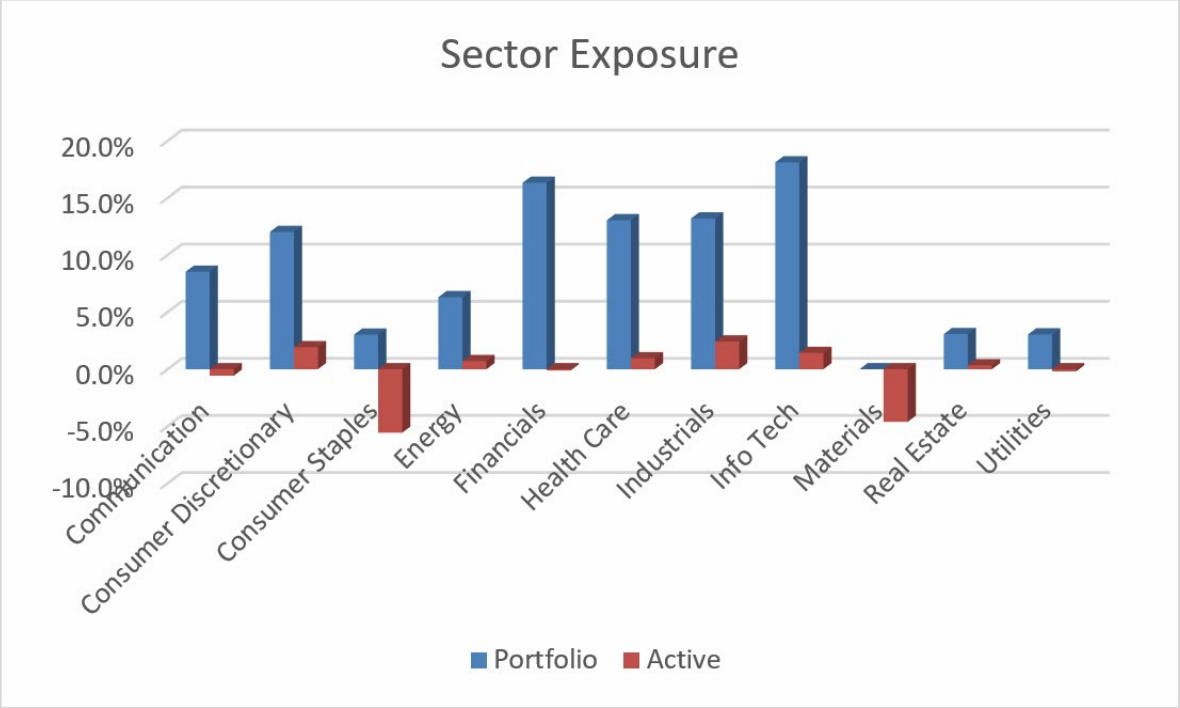
that the cycle could have many years left to run given the subdued nature of the recovery.

Top contributors to the year-to-date performance of the Ninepoint Focused Global Dividend Class by sector included Information Technology (+475bps), Industrials (+318 bps) and Communication (+212 bps) while no sector had a negative contribution on an absolute basis. On a relative basis, positive return contributions from the Industrials, Information Technology, Communication, Real Estate and Utilities sectors more than offset negative contributions from the Consumer Discretionary, Financials, Materials, Consumer Staples, Health Care and Energy sectors. Note that the underperformance in the Materials sector was primarily due to a sector allocation decision as opposed to individual stock picks.



Source: Ninepoint Partners

We are currently slightly overweight the Industrials, Consumer Discretionary, Information Technology and Health Care sectors while underweight the Consumer Staples, Materials and Communication sectors. Although we avoided chasing the sectors and stocks most sensitive to a positive resolution to the US-China trade war given the more deeply cyclical nature of these businesses (and therefore underperformed during the month), we are well positioned should trade concerns or fears of an economic slowdown return.



Source: Ninepoint Partners

At the stock specific level, top contributors to the year-to-date performance included Mastercard (+180 bps), Microsoft (+177 bps) and Visa (+115 bps). Top detractors year-to-date included Anthem (-56 bps), Citigroup (-34 bps) and Union Pacific (-25 bps).

In July, our top performing investments included Northrop Grumman (+24 bps), Medtronic (+18 bps) and Mastercard (+15 bps) while Kering (-36 bps), Thermo Fisher Scientific (-16 bps) and Allianz (-8 bps) underperformed.

Over the past few years, we have held various positions in the aerospace & defense sector. Our current top holding, Northrop Grumman (NOC), has been particularly strong since reporting its first quarter results last April. The shares continued to rally after the Company reported its second quarter results on July 24, with the stock jumping approximately 6% on the day. In a world where growth is becoming harder and harder to come by, NOC's 19% revenue growth (boosted by the inclusion of the recent acquisition of Innovation Systems) and 12% diluted earnings per share growth in Q2 2019 compared very favourably to most of the other stocks in our investable universe.

We expect operating and financial results to remain solid through the balance of the year given the 10% increase in backlog (to $63 billion), implying net awards in the quarter of $13.5 billion and a book to bill ratio of 1.6x. Consistent with this solid start to the year, management boosted guidance for 2019, bumping operating margin guidance (from a range of mid to high 10% to a new target of high 10%) and adjusted EPS guidance (from a range of $18.90 to $19.30 to a new range of $19.30 to $19.55). With $2.6 to $3.0 billion of free cash flow expected in 2019, it was not surprising that the Company increased its quarterly dividend 10% to $1.32 per share last May.

After trading at a significant discount to the aerospace & defense sector, based on next-twelve-month consensus earnings estimates (the spread reached almost five multiple-points just prior to the release of the Q1 2019 results), the recent rally in NOC has completely closed the valuation gap to its peers. Although the current valuation is still well-below the peak multiples reached at the end

of 2017, we need to be mindful that much of the forward earnings growth may have been priced-in. Should our investment process dictate an adjustment given market conditions, we may look to trim, sell or swap the position.

The Ninepoint Focused Global Dividend Class was concentrated in 29 positions as at July 31, 2019 with the top 10 holdings accounting for approximately 41.0% of the fund. Over the prior fiscal year, 26 out of our 29 holdings have announced a dividend increase, with an average hike of 13.0%. We will continue to apply a disciplined investment process, balancing various quality and valuation metrics, in an effort to generate solid risk-adjusted returns.

Jeffrey Sayer, CFA

NINEPOINT FOCUSED GLOBAL DIVIDEND CLASS - COMPOUNDED RETURNS[1]
AS OF FEBRUARY 29, 2020 (SERIES F NPP137)

	1M	YTD	3M	6M	1YR	3YR	INCEPTION
Fund	-5.8%	-3.8%	-4.8%	-3.8%	6.5%	6.7%	5.9%
Index	-6.8%	-5.8%	-4.9%	2.5%	7.4%	8.5%	8.7%

[1] All returns and fund details are a) based on Series F shares; b) net of fees; c) annualized if period is greater than one year; d) as at July 31, 2019; e) 2015 annual returns are from 11/25/15 to 12/31/15.

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